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<b>REPORT TO:</b>	<b>Council</b>
<b>DATE OF MEETING:</b>	<b>Oct 4, 2021</b>
<b>SUBMITTED BY:</b>	<b>Jonathan Lautenbach, Chief Financial Officer</b>
<b>PREPARED BY:</b>	<b>Jonathan Lautenbach, Chief Financial Officer</b>
<b>WARD(S) INVOLVED:</b>	<b>All Wards</b>
<b>DATE OF REPORT:</b>	<b>Oct 1, 2021</b>
<b>REPORT NO.:</b>	<b>FIN-2021-56</b>
<b>SUBJECT:</b>	<b>Proposed Merger Between Kitchener Wilmot Hydro and Waterloo North Hydro</b>

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## **RECOMMENDATION:**

**That the Memorandum of Understanding regarding a proposed merger between Kitchener Wilmot Hydro and Waterloo North Hydro, attached as appendix B, be approved**

## **REPORT HIGHLIGHTS:**

- A proposed merger between Kitchener Wilmot Hydro and Waterloo North Hydro was announced on October 1, 2021
- The City of Kitchener is the majority shareholder of KWH and any proposed merger requires shareholder approval
- A Memorandum of Understanding has been prepared that outlines the main elements of a merger between the two utilities
- The City of Kitchener would hold a 53.39% ownership share in the new entity under the proposed merger

## **BACKGROUND:**

Kitchener Wilmot Hydro (KWH) and Waterloo North Hydro (WNH) have been in discussions regarding moving forward with a proposed merger of the two utilities. A public announcement regarding the proposed merger was made on October 1, 2021. The City of Kitchener is currently the majority shareholder of KWH with a 92.25% ownership share and as such, any merger involving KWH would require City of Kitchener approval.

Under a proposed merger, the City of Kitchener would continue to be the majority shareholder of the larger newly formed entity with a 53.39% ownership share.

A Memorandum of Understanding (MOU) has been developed between all parties that outlines the main elements of the proposed transaction. The MOU is a non-binding agreement that helps set the general understanding and expectations regarding the

proposed merger. Following approval of the MOU by municipal shareholders, a public engagement process will launch on October 5, 2021 giving the public an opportunity to learn more about the proposed merger and to provide feedback. It's anticipated that final approval from municipal shareholders to proceed with the proposed merger would be requested through a separate report that would come back to Council for consideration in December 2021.

The Boards of the respective utilities support proceeding with a merger of the two utilities and approval of the MOU is being requested from the municipal shareholders of KWH and WNH.

## **REPORT:**

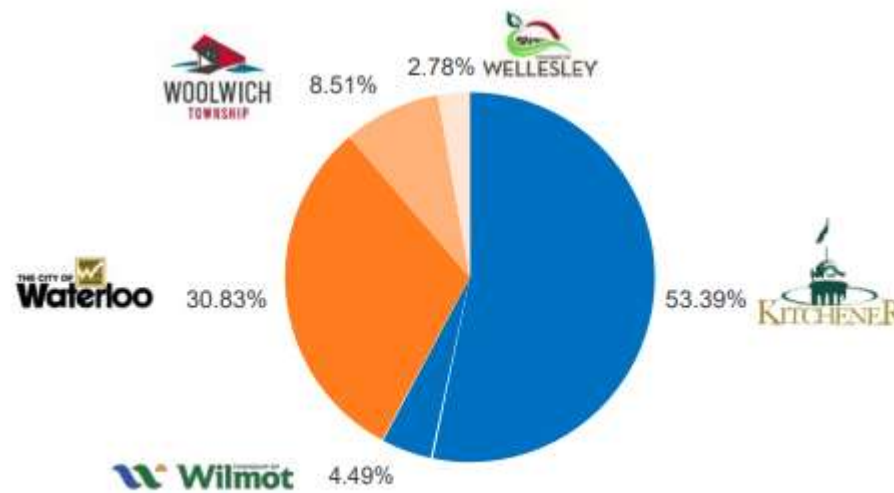
The electricity distribution landscape in Ontario has been changing, with more mergers and acquisitions taking place involving Local Distribution Companies (LDCs) in recent years. Recent and proposed transactions include Veridian and Whitby Hydro, Guelph Hydro and Alectra, Peterborough Hydro and Hydro One, Orillia Power and Hydro One, Energy Plus and Brantford Power. This trend in mergers and acquisitions is a result new regulatory and policy changes that has made merger opportunities more attractive for LDCs. In addition, consolidation of LDCs has been encouraged by the Province in order to ensure stable and reliable energy distribution for communities across Ontario.

KWH and WNH have been in discussions regarding a potential merger and the potential benefits that it could provide for the two utilities. Grant Thornton was engaged by the utilities to explore what a potential merger may look like and to better understand the benefits that it could provide, both from an individual utility and an existing shareholder perspective. Municipal shareholders were engaged early in the process as any merger involving both parties would require approval of municipal shareholders.

The City of Kitchener is currently the majority shareholder of KWH with 92.25% ownership share. The Township of Wilmot is the minority shareholder with a 7.75% equity stake.

The City of Waterloo is currently the majority shareholder of WNH with a 73.2% ownership share. The Township of Woolwich and Township of Wellesley own 20.2% and 6.6% equity stake respectively.

Under the proposed merger the ownership share for municipal shareholders would be adjusted as follows:



Kitchener will remain a majority shareholder of the new utility with a 53.39% ownership share. Making sure that the new entity continues to be locally owned is an important consideration. By merging with WNH now, it is expected that the new utility will remain responsive to community and customer needs.

As indicated in the summary of comments provided by Grant Thornton (see Appendix A), a merger between KPC and WNH would result in the 7th largest LDC in Ontario. The MOU attached (see appendix B) outlines several objectives/benefits that the merger between KWH and WNH is expected to achieve:

- Customers will enjoy ten-year distribution rate stability and distribution rates as low or lower than in a standalone alternative
- Distribution rates of the former KWH and WNHI service territories will harmonize over time
- Continued excellence in customer service
- Total cost savings to be shared amongst the Municipal Shareholders and customers
- Stronger and more sustainable cash flow to Municipal Shareholders via interest and dividends
- The ability to dedicate significant leadership and focus on innovation and growth
- A larger entity with a stronger balance sheet capable of supporting future growth
- Improved service reliability leveraging best practices and capabilities of both LDCs
- A stronger energy and infrastructure partner for local businesses and communities
- Alignment with provincial government policies encouraging consolidation in the electricity distribution sector
- Increased ability to access financial and other resources available to invest in non-regulated energy services, businesses and solutions for customers

From a shareholder perspective, the newly formed utility will provide additional dividends for Kitchener which are outlined in the financial implications section of this report. These additional dividends will be allocated through the City's annual budget process.

Proceeding with a merger between KWH and WNH will ensure that customers of both utilities continue to receive reliable service at competitive rates , both now and in the future.

Jerry Van Ooteghem, CEO of KWH, and Jim Phillips, KPC Board Chair, will be in attendance to provide a presentation for Council and answer any questions that Council may have regarding the proposed merger.

**STRATEGIC PLAN ALIGNMENT:**

This report supports the delivery of core services.

**FINANCIAL IMPLICATIONS:**

The City of Kitchener currently receives approximately \$6 million in annual dividends and interest from KWH.

Under the proposed merger it is estimated that the City of Kitchener will receive incremental returns of \$9.6M over a 20-year timeframe.

In addition to the incremental returns that are a direct result of a proposed merger, a dividend policy change that would be required to align with WNH's dividend policy will provide an increase of an estimated \$28.9 million for Kitchener over a 20-year timeframe.

Dividends from ownership of the hydro utility are allocated through the City's annual budget process help address both the City's operating and capital need.

**COMMUNITY ENGAGEMENT:**

INFORM – This report has been posted to the City's website with the agenda in advance of the council / committee meeting.

The approval of the MOU will start the public engagement process regarding the proposed merger. A website [connectinglocalpower.ca](http://connectinglocalpower.ca) has been set up for members of the community to learn more about the proposed merger and to provide their feedback.

**APPROVED BY:** Dan Chapman, CAO

**ATTACHMENTS:**

Appendix A – Business Case - Summary Comments from Grant Thornton LLP  
Appendix B – Memorandum of Understanding